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RUEHLE/AMEMBASSY LUXEMBOURG 0009  
RUEHMN/AMEMBASSY MONTEVIDEO 1944  
RUEHSG/AMEMBASSY SANTIAGO 1684  
RUEHRG/AMCONSUL RECIFE 2885  
RUEHRI/AMCONSUL RIO DE JANEIRO 7050  
RHEHNSC/NSC WASHDC  
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UNCLAS SECTION 01 OF 03 SAO PAULO 000464

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TREASURY FOR OASIA  
USDOC FOR 4332/ITA/MAC/WH/OLAC  
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TAGS: [ENRG](#) [EPET](#) [EINV](#) [ECON](#) [PGOV](#) [PREL](#) [BL](#) [BR](#)  
SUBJECT: MULTINATIONAL'S CONCERNS ABOUT BOLIVIAN GAS  
NATIONALIZATION

REF: A. 05 SAO PAULO 735  
[1](#)B. 05 SAO PAULO 789  
[1](#)C. SAO PAULO 152  
[1](#)D. BRASILIA 754

[1](#)1. (SBU) Summary: The Sao Paulo-based head of British Gas (BG) for South America expressed grave concerns about the May 1 Bolivian Government decree nationalizing natural gas production. Brazil's Petrobras was hit the worst of all the multinational companies, losing much of its revenue stream in Bolivia's largest gas fields and losing control of its two refineries. Waddell predicted a muted international reaction as companies await further definition of the decree's vague provisions. Should foreign companies leave or be expelled, Bolivia has the capacity to continue current production by coercing Bolivian hydrocarbons industry workers to stay on and importing Venezuelan industry executives. Bolivia will likely continue sending natural gas to Brazil, which has recently tested provisions to reduce gas consumption if need be. Production in Brazil's Santos Basin, which has the potential to replace Bolivian gas, will not start production until 2009 at the earliest. End Summary.

Evo's Masterful Maneuver

[1](#)2. (SBU) During a May 2 conversation, BG Executive Vice President for South America Rick Waddell told Econ/Pol Chief that Bolivian President Evo Morales had been very politically astute in how he issued the May 1 (May Day) decree "nationalizing" hydrocarbons production, raising taxes to 82 percent in Bolivia's two mega fields (run by Petrobras, Repsol, and Total), and regaining state control of capitalized companies (including the Transredes pipeline company operated by US company Prisma, and the two EBR refineries run by Petrobras) with no mention of compensation. Waddell noted that Evo had originally wanted to issue the decree mid-April (during Holy Week) but had delayed after

Petrobras complained about the lack of consultation. The Bolivian Government sent senior hydrocarbons officials (including Minister Solis) two times to Brasilia for talks, which went badly since the Bolivians simply told the Brazilians they had to be willing to work in Bolivia as mere service providers. Nonetheless, Waddell continued that Petrobras and the other hydrocarbons companies could not believe the Bolivian Government would actually do what Morales said he would do (and in the process turning its back on future investment from Brazil), a complacency encouraged by conciliatory public statements by the Bolivians through last week. According to Waddell, the decree, which was harsher than expected, was driven by ideology and meant to help Morales consolidate himself in power by coming two months before elections for Bolivia's constituent assembly, which Morales hopes will rewrite the country's constitution a la Chavez in Venezuela.

#### Big Blow to Brazil

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13. (SBU) Waddell characterized the decree as a slap in the face of Brazil, one of the countries that has been most supportive of the new Morales administration. The fact that the Brazilian Government recalled both Foreign Minister Amorim and Petrobras President Gabrielli from abroad shortly after the decree's issuance is indicative of how concerned the Brazilians are. One potential carrot in the decree that the Bolivians will likely use on Petrobras is the offer to "audit" companies in the megafields on a case-by-case basis and offer some rebate of the huge 82 percent tax bill. Waddell noted that the decree leaves many questions

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unanswered on procedures and definitions, including what will happen with Petrobras' refineries.

#### Muted International Reaction

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14. (SBU) Waddell predicted little concrete reaction by the international community to the nationalization decree. As previously reported, the multinationals had all sent "trigger letters," which allege non-compliance of contracts by the Bolivian Government and enable any of the companies to start international arbitration cases against Bolivia. (Note: Our understanding is that Petrobras never sent a trigger letter. End Note). He doubted any of the companies would begin arbitration yet, preferring to see how events unfold. This lack of action, in turn, emboldens Morales, who thinks he can emulate what Chavez did to the companies in Venezuela. The difference, asserted Waddell, is that the companies in Venezuela had already invested tens of billions of dollars there and could not afford to walk away. Bolivia, on the other hand, is at the beginning of its investment cycle (now frozen), and the multinationals could afford to walk away if need be. For example, Bolivia provides just two percent of BG's world production, and their total investment there is about ten percent of BG's annual profit; a hit, but not fatal.

#### With Venezuelan Help, Bolivia Can Maintain Production

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15. (SBU) Waddell believes that even if the multinational companies leave Bolivia or are kicked out, the Bolivians will be able to keep up current production, though not do any new investment. While YPFB, the Bolivian state hydrocarbons company, does not have enough qualified technicians to keep things running, enough Bolivian workers could easily be found at the multinationals. In BG's case, there are only three foreign executives in the country, with the rest being Bolivian nationals. The Bolivians could be coerced into staying on once the "imperialists" were gone and work for YPFB, or they would be unemployed, or even jailed as "traitors." Executives from Venezuelan state hydrocarbons

company PDVSA could replace the expelled foreign executives. Waddell recounted BG's recent experience, when YPFB wanted to check out a BG field ostensibly to inquire about bottled natural gas. In reality, the visit was to check on the whole operation, with only two YPFB employees showing up along with a dozen PDVSA employees wearing their company work clothes. The PDVSA workers insulted the BG Bolivians, telling them they will soon have to wear a Venezuelan flag over the Bolivian flag on their work clothes.

#### Unlikely to Hurt Brazil's Gas Supply

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¶6. (SBU) While difficult to predict the decree's impact on Brazil's natural gas supply, especially given the Morales administration's unpredictability, Waddell doubted that Bolivia would try to cut off or reduce the supply of gas to Brazil. Bolivia needs the revenue from Brazilian sales too much, as well as the petroleum for the domestic market that can only be produced in conjunction with natural gas. Waddell also doubted the Bolivians would unilaterally try to raise the price of gas to Brazil given that the contract regulating the price was signed under New York law and would generate the same problems of reduced revenue if the Bolivians tried to reduce or cut off Brazil's gas supply. Waddell used Brazil's recent actions after the gas supply from Bolivia was reduced from a landslide-damaged pipeline as an example of what Brazil could do to mitigate the effects of

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reduced supply. The current pipeline has a capacity of 30 million cubic meters (mm3) per day, and Brazil was taking 26 mm3 before the accident in March dropped the flow to 21 mm3. To make up for the missing 5 mm3, the Brazilians decreased thermo-electric electricity generation using gas and switched the power used to run two major Petrobras refineries in Brazil. This resulted in enough energy savings to allow other industries to continue to use gas during this period. Although it will take another 30-60 days to finish repairs to the pipeline in Bolivia, most of the missing gas has already been made up through bypasses. If further gas use reduction is needed, Brazil can raise taxes on natural gas use in vehicles and lower taxes on gasoline use.

¶7. (SBU) Regarding the potential gas reserves in Brazil's Santos Basin, Waddell noted that the Brazilian Government publicly states that production will begin by 2008, a ploy used to pressure Bolivia. The industry (including candid Petrobras officials), however, knows that production cannot begin until 2009 at the earliest. The Basin can eventually produce 30 mm3, enough to replace the Bolivian gas supply, and perhaps even more as exploration continues (the exploration-to-production phase takes 3-5 years). Waddell also discussed how Bolivia could increase production to maximize the 30 mm3 capacity of the pipeline, should Brazil need more gas before Santos is on-line. Even in the poor current investment climate in Bolivia, companies could be willing to invest more money in Bolivia to bring fields relatively easily and cheaply into production. However, no one is willing to invest in new production development or build new pipelines.

#### Bolivia's Lost Opportunities with Other Neighbors

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¶8. (SBU) Bolivia is currently selling 4-6 mm3 to Argentina on interruptible contracts, which Argentina would like to make permanent and increase in volume. While this could be a windfall for Bolivia, Waddell does not foresee needed investment materializing to take advantage of this demand. Chile, which would normally be a good customer for Bolivian gas were it not for political problems, will import more expensive liquefied natural gas (LNG) via a BG regassification plant.

¶9. (U) This cable was coordinated with Embassies Brasilia and

La Paz.  
MCMULLEN